

# CSD Research Report

## **ADD: Lessons from the UK**

Dominic Maxwell and Will Paxton

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# **ADD: Lessons from the UK**

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The UK's matched savings scheme is growing rebellious. Inspired by the American Dream Demonstration (ADD), the UK is now on its second set of pilots – but the subtle differences introduced in the first set are becoming gradually more pronounced. The programme is growing up, asserting its independence from its American parents and experiencing all the angst of adolescence.

The differences between the US and the UK are particularly concentrated in the role of community organisations, the match rate, and restrictions on how the money is used. This paper asks what lessons are revealed by these three US/UK differences. In asking, it becomes apparent that there is a fundamental question over the purpose of matched savings accounts: are they intended to develop a savings habit, build up an asset stock, or assist the purchase of specific items? In the UK, the emphasis is more on the savings habit and the assets buffer than it appears to be in America, but in different areas of programme design the tensions between objectives are acute.

## **Box 1: About the Saving Gateway (SG)**

The first round of pilots in the Saving Gateway (SG1) was explicitly inspired by the American Dream Demonstration. Of the five different pilots, four were run in partnership with community-based organisations and were linked to financial education.

But from the start, there were important differences between the American and British versions. The match rate for the Saving Gateway was only 1:1, and there were no restrictions on how the money could be spent. The Saving Gateway was on a smaller scale, run in only five locations with a total of 1,500 participants. Participants could save up to £25 per month, with a total maximum over 18 months of £375.

In early 2005 a second round of pilots was launched (SG2). SG2 increased the number of locations from five to six, the number of people from 1,500 to 20,000, and the maximum income from \$15,000 (\$27,300) to £25,000 (\$45,500).<sup>1</sup> The second round of pilots also varies the match rate, with pilots at 1:1, 1:2 and 1:5. The last account will graduate the programme at the end of 2006, although they will automatically stay open (without matching) after this time.

## **1. The role of community organisations**

Four of the five pilots in the first round had heavy involvement from community organisations. Three were housing associations (non-profit providers of social housing, funded by government), and one, Toynbee Hall, was a community anti-poverty organisation, similar to - and in fact the inspiration for - Chicago's Hull House. These organisations recruited participants, fielded enquiries, helped clients fill

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<sup>1</sup> Exchange rate correct as at 10/6/05

in forms, and ran complementary financial education. The fifth pilot, in Hull, simply sent potential participants a letter from central government informing them of their eligibility and inviting them to contact the bank.

The community organisations certainly provided an important service. They were able to recruit participants who were more deprived than in Hull, with twice as many having a household income over £100 per week, and less than half as many earning over £200 per week. Hull participants were less likely to be unemployed and looking for work (although they were more likely to be unable to work due to ill health), and were 17 percentage points more likely to have a current account before joining (87 per cent compared to 71 per cent).

But the organisations' involvement was still shallow compared to similar organisations in the ADD. The pilots were designed by the Treasury, their timing and size dictated, and the space in which organisations could innovate was tightly constrained, rarely extending beyond recruitment and education. Rather than submitting proposals for funding, organisations were invited to bid for a contract. The initiative, in other words, ran in the opposite direction.

For the second round of pilots, SG2, the role of community organisations will be reduced still further. Recruitment will be along the lines of the Hull technique, sending letters and waiting for participants to present themselves. Every pilot site has locally-provided financial education linked to the SG, but providers are unable to use the government list of eligible individuals and so are unable to contact participants directly.

SG2 is designed to be one step closer to a national roll-out, and it was thought that the community-led model did not offer a realistic pathway to scale. The voluntary and community sector often fills a different function in Britain than America, focusing less on the direct provision of welfare. Certainly government-funded faith-based initiatives, such as those developed by President Bush, are absent in Britain (at least partly because the government itself provides greater levels of support). Social housing organisations could in theory fill some of the gap, but although every area has some provision of social housing, this is sometimes through the independent housing associations and sometimes through local government, varying street to street according to local history and circumstances. The large housing associations have increasingly good coverage, but still only include part of the social housing sector. Focusing just on housing associations would also exclude many thousands of people who would benefit from the programme but do not live in social housing: according to one study, half the poor are homeowners (Burrows and Wilcox 2000).

Rolling out the community-led model would also be far more expensive. In the long run the extra innovation may make it a price worth paying, but it is plausible that the benefits of innovation decline as thinking on individual development accounts becomes more mature. If this is true, then the best course of action may be to move from a highly localised structure, such as ADDs, to a more centralised one as time passes.

The involvement of community organisations, then, may be a necessary casualty. The calculation must take account of how important it is to provide a pathway to scale,

how much innovation community groups provide, whether there are alternative ways of recruiting poorer and more deprived individuals, and to what extent policy-makers are willing to divert resources from asset-building towards the broader education and involvement that community organisations can deliver.

## 2. How high a match?

The match rate of SG1 was relatively low compared to many ADD programmes, at 1:1. SG2 is even lower, varying down to 1:5. Is that too low? Are the Brits just mean? To think about what the “correct” match rate might be, we need to look again at the basic motivations for the programme, and at the possible distortions the match might induce.

As mentioned above, the motivation for SG puts more emphasis on process than the American equivalents do: the point is not simply to *own an asset*, but to *develop a savings habit*. If developing a habit were the sole motivation, then the match rate ought logically to be as low as is consistent with encouraging participation. Given the extra opportunity cost of saving for the poor, and the extra institutional and cultural barriers that may prevent them starting, this motivation would also suggest that the poorer the target group, the higher the match rate that is needed.

The 1:1 match rate of SG1 does appear to have been high enough to kick-start a savings habit. Participants made a deposit on average in 71 per cent of months, and depth interviews for evaluation indicated that most participants developed savings habits they were reluctant to break, so saved even when they had difficulties. Three months after the programme finished, 91 per cent still had their account open and 41 per cent were still saving regularly. Many of those who were continuing to save attributed it to the routine that they had developed through SG (Kempson et al 2005).

In fact, the 1:1 may if anything have been too high, slowing recruitment with suspicions that the offer is “too good to be true”. Recruitment in Hull increased when the government logo was made larger, perhaps suggesting that potential participants were in need of reassurance. The following quotes from participants, taken from evaluation interviews, are enlightening:

*I read the stuff first and I was a bit, it seemed too good to be true at first. When they say the government will double your money, it just seems too good to be true. I was looking for the small print.*

*As soon as I read that you were going to get 100% profit on the money paid in, I mean everybody I have spoken to about it says ‘Where is the catch?’ I said ‘I don’t know, I’m frightened to death what the catch might be’.*

Kempson et al, 2005: 35

If people are “frightened to death” that the offer is too attractive, it is not hard to imagine a smaller match rate being at least as effective. So the UK experience suggests a match rate of 1:1 is certainly high enough, and may be too high. The second pilots will show us the effect of a lower rate: who (if anyone) will reduce their saving habit in response, and who will not participate at all?

A second motivation of the programme might be to provide individuals with the security and other benefits that come from asset ownership – the set of benefits known as “the asset effect”. By preventing the worst vulnerabilities of poverty, assets are thought to be able to increase the propensity to plan, the ability to take productive risks, and the strength of “self-efficacy” – the extent to which individuals feel they can change their own situations through their actions. SG1 gives some support to this idea: 29 per cent, for example, agreed or agreed strongly with that participation had left them “more in control of my own life” (50 per cent neither agreed nor disagreed).

Crucially, though, other research appears to suggest that there is a relatively low cut-off point, around £300-£600 (\$550-\$1,100), after which extra savings do not bring extra benefits (Bynner and Paxton 2001). The asset effect is an important justification for state involvement: by pointing out the effects on planning, vulnerability and attitudes, narrow interpretations of microeconomic analysis can be exposed as incomplete. But once participants own more than £300-£600, if it is true that the asset effect fades, it becomes much easier to argue that the decision to save or spend money should be left to the individual. How this target figure gets translated into a match rate depends, of course, on the length of the programme and the monthly maximum, but the SG’s overall limit of £375 appears sufficient.

Finally, the motivation might be to help individuals to pay for specific purchases, such as a house or education. In that case, the match is in some ways more similar to a subsidy for that particular good, rather than just a savings policy, and the appropriate match would depend on the social benefit that the good provides.

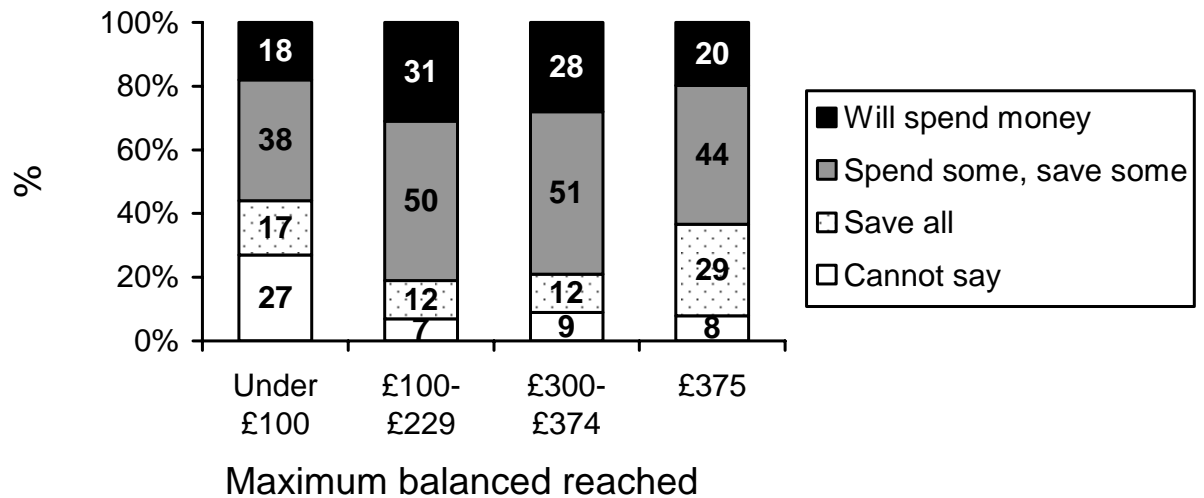
Turning to distortions, the higher the match rate, the more incentive it provides to borrow in order to make deposits. The UK experience with a 1:1 match is encouraging on this: less than 0.5 per cent said they had funded their deposits through commercial borrowing, although 3 per cent borrowed from a family or friend and 5 per cent transferred money from a savings account. Again, it will be interesting to see how these figures vary under the different match rates in SG2.

### **3. Restrictions or no restrictions?**

The Brits are mean with their match rates, but generous with their lack of restrictions: after going through SG, participants can spend all the accumulated funds on whatever they see fit. This partly reflects the emphasis on the savings process, promoting a savings habit rather than a stock of wealth. It is also made more possible by the lower match rate. Yet the contrast between Britain and America is still instructive, with many people finishing SG with no clear idea of what the funds will be used for.

How well used are the funds? Do they actually remain as a savings buffer, or are they all spent straight away? The graph below shows the spending/saving intentions of participants, as reported in the questionnaire at completion (Kempson et al 2001: 77).

## Uses of SG savings



This graph tells us that the majority of people (depending on how much they saved) were left with some asset base at the end of the programme. This would be consistent with the idea of assets as a reserve, bringing security and allowing people to plan ahead: the asset is providing a valuable benefit even if it is not being used. The interim evaluation of SG1 pointed out that those intending to keep their money for a rainy day were the largest group. Most, but “by no means all” of these people had identified themselves as rainy-day savers at the start of the programme (Kempson et al 2003). It should be noted, though, that only thirty people were interviewed in depth and those intending to keep their money would be a still smaller subgroup.

The money that was withdrawn may or may not have been well used – the graph alone is unable to help us. If all participants withdrew their money for day-to-day living expenses then the programme would have failed to promote wider asset ownership. If, on the other hand, it was spent on education or lumpy purchases (such as a cooker), and/or a broader savings habit had been developed, then it certainly would be a success. Of those who were interviewed in depth for the interim evaluation, those who intended to spend all the money (both savings and match) were most likely to be saving for a holiday; others wanted things for their home that they could not otherwise afford; one person was saving up to replace her car. The small sample size is again important.

While a holiday may not be the most socially-desirable purchase, in general there is not a clear boundary between “worthy” and “unworthy”, whether this is interpreted as “investment” versus “consumption”, or smoothing versus everyday expenditure. A purchase for one person may be an important way of smoothing a crisis and preventing unsustainable debt spirals, but the same purchase by someone in different circumstances may be part of regular spending. Similarly, it may be an important

investment in personal development, or a luxury with no long-term benefits – a car, for example, could be either, depending on whether it is purchased to travel to work or cruise the high street. Without also knowing the wider circumstances, it is hard for researchers (or those who design restrictions) to see in advance how well the money is being used.

What the graph does tell us, though, is that a high proportion of people had no specific plans for their savings, particularly if those who “cannot say” are interpreted as not having plans. It would be a reasonable conjecture that restrictions would put people off participating either if they had firm intentions that were not permitted by the restrictions, *or* if they had no plans for the money but wished to preserve flexibility. Imposing restrictions could then reduce the ability of the programme to promote a savings habit by reducing the number of people who wish to take part.

#### **4. Conclusion and next steps**

The close similarities between the US and the UK programmes make the differences all the more enlightening. Some of them can be explained by their different social and political environments. The reduced role of trusted intermediaries, for example, is at least partly a response to a different structure of community organisations in the UK. But the UK’s experience still poses some challenges for schemes in other countries, and still has much to learn from the ADD and its equivalents. On community organisations, a more centralised structure may offer greater cost efficiency and a clearer route to national roll-out, but possibly at the expense of innovation. The match rate of 1:1 appears sufficient to provoke a savings habit – and higher rates than this run a greater risk of introducing distortions, such as commercial borrowing to take advantage of the match. The second round of pilots, due to finish at the end of 2007, will show to what extent the match can be reduced still further without reducing effectiveness. And finally, on restrictions, the UK’s experience suggest that many people enter the programme with no fixed ideas as to how to spend their savings, and preserving sufficient flexibility to allow this may be important for recruitment. How these various tensions are resolved depends on how we balance the different motivations for matched savings.

The second round of pilots will allow us to examine these issues in more depth. Depending on their results, we will see whether the UK’s small divergence is temporary – a soul-searching adolescence followed by a return to the family traditions – or a longer-term parting of ways. Either way, transatlantic conversations are likely to be mutually productive for a considerable time to come, and the Centre for Social Development has our gratitude for its continuing role in arranging them.



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